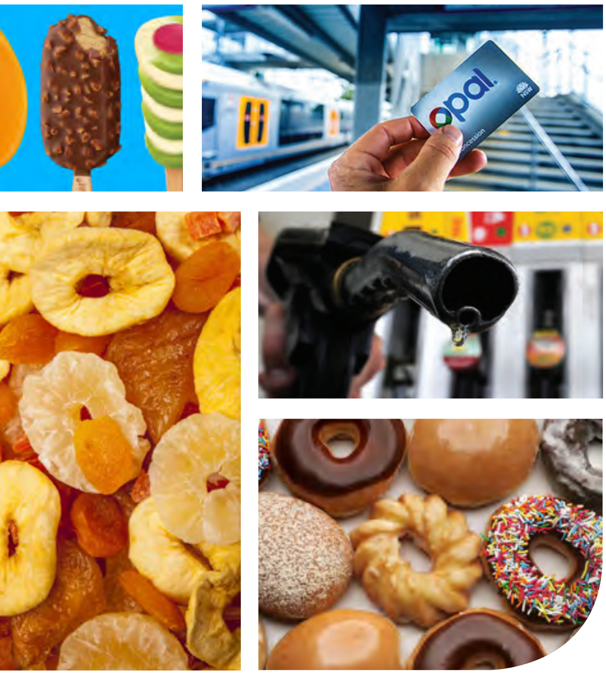
AACS

AUSTRALASIAN ASSOCIATION OF CONVENIENCE STORES

Established 1990

2017 State of the Industry Report

Contents



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INTRODUCTION

We are pleased to bring the 2017 AACS State of the Industry report to you.

This report continues to be a sought after publication by retailers, suppliers, regulators, analysts and the media as it is the most credible insight into the Australian convenience industry.

I again thank the retailers who took the time to provide data to enable us to publish this year's report. In addition, I thank Daniel Bone and the team at IRI for their insights and excellent work in once again compiling this year's report.

I also thank our major sponsors of this year's AACS State of the Industry Report, Coca-Cola Amatil and Imperial Tobacco Australia.

As you will read further in this report, 2017 saw convenience in-store merchandise sales grow by 1.0% in tough retail conditions. The bright spot is the fact that food and beverages continue to grow in our channel, which is a reflection of the work done by many of our retailers and suppliers.

We should continue to have 'confidence in convenience' but also need to keep reviewing our offer and innovation platforms to ensure that our industry is being seen as a credible destination for emerging categories such as food and beverages.

AACS remains committed to our pillars of Representation, Innovation, Communication and Education.

We will continue to advocate for our industry in areas affecting the things that matter to our members and could affect them either positively or negatively.

COCA-COLA AMATIL

Imperial Tobacco

IRi Growth delivered.

1.0%

Convenience in-store merchandise sales grew in 2017

Food and beverages continue to grow in our channel

Jeff Rogut
FAIM, MAICD, FCLP
Chief Executive Officer
Australasian Association of Convenience Stores Limited
ACN: 156 638 023

Your AACS Board members

Retail Member Directors of AACS

- Jeff Rogut, CEO AACS
- Chair: Julie Laycock, 7-Eleven
- Vice Chair: Rob Anderson, APCO
- Treasurer: Chris Andrianopoulos, AA Holdings
- Amanda Woollard, BP
- Darren Park, UCB
- Steve Cardinale, New Sunrise Group
- Anisa Makalic, Caltex
- Jennifer Gray, VIVA Energy

Supplier Member Directors of AACS

- James Lane, Coca-Cola Amatil
- Caroline Waite, Frucor
- Brett Barclay, Convenience Measures Australia

In 2017 these were just some of the AACS activities that took place:

- AACS Annual State of the Industry Report Launch
- AACS Downunder Study Tour to Melbourne
- AACS Convenience Leaders Summit and AACS Gala and Awards dinner in Sydney
- AACS Collaboration and Innovation workshops
- AACS Overseas Study Tour to the USA
- AACS PJ Convenience Industry Award
- AACS Women in Convenience events
- AACS Weekly eNewsletter publication
- Regular submissions to government on issues that affect our industry such as tobacco regulations, sugar tax, container deposits, illicit tobacco, menu labelling etc

Looking ahead

Looking ahead to 2018 and beyond we continue to

focus on regulatory issues

that could either positively or negatively affect the convenience industry

Long a source of frustration for retailers, unnecessary and onerous regulations can dampen trade and affect small businesses' ability to compete with the major supermarkets and other retailers. To counter, we have signalled our intent to focus on several key legislative and regulatory issues in what is an election year in some states.

Addressing the various factors that impact the cost of doing business for small retailers like convenience stores is a key focus and these are broad reaching.

Factors like increases to the minimum wage, excessive taxes on products like legal tobacco, and the lack of choice for small retailers in processing tap-and-go payments all increase pressure on the cost of doing business while failing to recognise the important role convenience stores and other small businesses play in the community and economically.

On the other hand, we have the major problem of crime in our industry. This issue is compounded by the inappropriate legislative and judicial response to those criminals who commit theft – or worse – as well as those involved in the illicit tobacco market.

These issues can make or break a convenience store's bottom line. So this year, the AACS is increasing pressure, rallying against unnecessary regulations, seeking stronger deterrents for criminals, and securing a better trading environment for small retailers like convenience stores.

Our Association will remain vocal and active on these issues and we encourage convenience retailers and suppliers, as well as other retail businesses, to have their voices heard on the issues that affect them.

This year is an election year in some states and while small business issues often struggle to gain the attention of politicians, the prospect of votes invariably does.

The cost of doing business

A plethora of factors influence the cost of doing business for convenience stores.

2 major areas have the potential to
significantly impact the bottom line
of small retailers in 2018

1 A push to raise the minimum wage through changes to casual employment

2 The lack of choice in processing tap-and-go payments

Proposals to increase the minimum wage in Australia will have a counterproductive impact, squeezing small businesses while limiting their ability to employ more people and, ultimately, threatening jobs.

Any push by the ACTU to change casual employment conditions and increase the minimum wage even further will have the opposite effect to that intended: increasing pressure on businesses, stifling growth and reducing employment opportunities.

It also fails to account for the fact that many people desire greater flexibility in their work hours and schedules.

At the same time we owe it to our people and communities to ensure that we are totally compliant with all legislation particularly as it applies to payments for staff. There is bound to be more, not less focus in this area, and the convenience industry has the opportunity to be seen as leading the way in cleaning up past issues and setting the benchmark for future positive action.

Tap-and-go card fees are another area under the spotlight this year

With tap-and-go payments becoming the norm, the cost of doing business for small retailers is impacted by the lack of choice to route these payments using the domestic eftpos system, so as to not incur higher international charges.

As it stands, payments on dual-network debit cards must be processed through either the Mastercard or Visa networks. These are international networks which cost small retailers more to process.

Having the option to route tap-and-go transactions through the eftpos network has the potential to save convenience stores thousands each year, but we need the banks to take notice and make this option available to these businesses.

+$

Tap-and-go costs small retailers more to process

Activism: Federal, state and local

The battleground of issues crucial to convenience stores getting a fairer go is drawn across Federal, state and local lines.

The AACS is urging retailers to contact their respective members, write letters, outline their perspectives and seek meetings to limit further regulations and restrictions on certain products

Some states are considering lifting the age at which people can buy legal tobacco from 18 to 21, yet at the same time want to continue to prevent eCigarettes – viewed internationally as a highly effective tool in helping people quit – from being legally sold. It's a classic example of regulation gone wrong.

At the same time, we have the periodic suggestions by the health lobby that soft drink taxes, sugar taxes or salt taxes are needed to improve societal health, yet convenience stores are already innovating with healthier food and beverage offerings and a more sustainable product profile.

We have a situation where the market for packaged alcohol is dominated by the two major grocery chains, new licences are granted to other big businesses like Aldi, but convenience stores are prevented from competing in this category.

It's an example of the lack of action at the local council level having an anti-competitive effect more broadly.

Less regulation, not more

We need less regulation, not more, to compete more effectively with the major grocery chains, so convenience stores should take the opportunity now to ask these questions of Federal, state and local politicians until a more appropriate operating environment is achieved.

Crime

The AACS has been vocal about the inappropriate response to crimes committed against the industry in recent times, and this will continue until the judicial response to these crimes matches the stance that the community demands.

We need tougher penalties and deterrents for the crimes committed against convenience stores and their staff to reflect their serious nature.

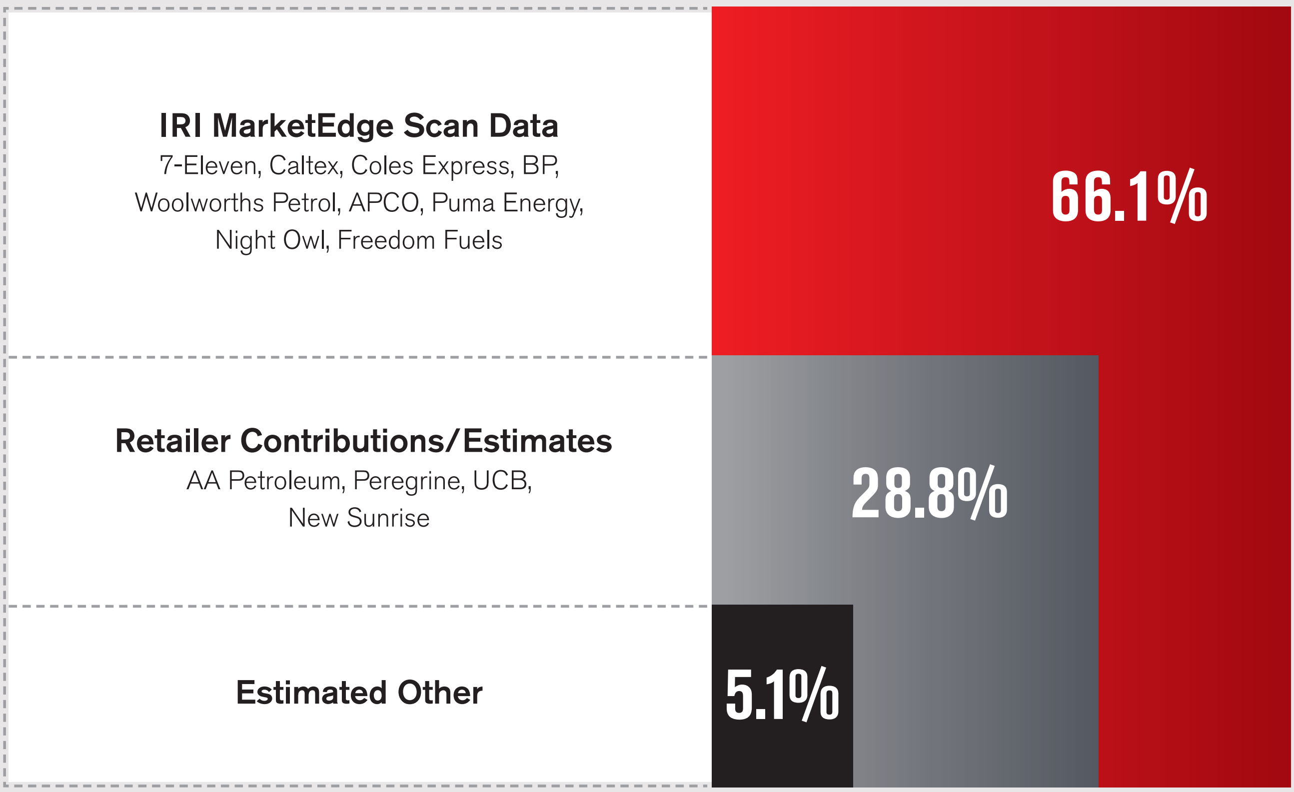
Robberies, petrol theft and the market for illicit tobacco all represent serious crimes which are not being dealt with in a satisfactorily serious way.

We will continue to press our case to those politicians with the capacity to alter the landscape and make the businesses in our industry, and the people who work in them, safe.

I thank all of our Members for their continued support of our industry, as well as the AACS Board for their work and dedication.

REPORT METHODOLOGY

- For the last 4 years, IRI have been appointed by the AACS board to compile the annual AACS State of the Industry (SOI) Report.
- The strength of IRI's MarketEdge scan market measurement (66% coverage) allows for the most robust and granular read of Australia's Petrol and Convenience (P&C) industry performance.
- Total industry and total category data presented in this report utilises IRI's actual retail sales scan data, combined with topline retailer sales performance collected from AACS retailer members.
- Not all P&C retailers are members of AACS, or are able to provide data across all areas of their business. As such, not all have provided data for this report.
- In instances where retailers are not able to provide data through either of these methods, a projection is included to represent their contribution to the P&C retail market.
- The headline performance metrics for each of the 20 categories profiled in this report are based on IRI's coverage, in combination with AACS member contributions derived from an industry survey.
- All segment and sub-segment performance data is based on IRI MarketEdge only (as clearly sourced throughout the report).
- Other data and research inputs such as the Australian Bureau of Statistics, Convenience Measures Australia and Roy Morgan are clearly referenced throughout.



TOTAL INDUSTRY

Dollar sales
$8.4 billion

DOLLAR GROWTH YA %	ACTUAL GROWTH ($ MILLIONS)
+4.5% 2016	+$353m 2016
+1.0% 2017	+$85m 2017

Shop visits per week **1.9%***

Margin **33.5%**

Source: IRI MarketEdge; AACS Member Submissions; *Convenience Measures Australia

Australia's petrol & convenience (P&C) industry recorded softer performance in 2017

- The $8.4 billion P&C industry (in-store sales only) posted lower dollar growth of 1.0% in 2017 (versus 4.5% in 2016).
- The $85 million revenue uplift amounted to $268 million less added value than in 2016.
- 13 of the 20 areas of in-store merchandise declined, and another was flat; by comparison, just 5 categories declined in 2016.
- Diminishing growth disrupts the consistent and robust upward trajectory recorded over the last 5 years, during which time in-store sales growth has oscillated between 3.4% and 4.5%.
- In-store merchandise performance in Australia mirrors the trajectory observed in the US market. The most recent NACS State of the Industry data revealed that declining c-store trips/traffic had contributed to in-store growth tapering off from +3.2% in 2016 to +1.7% in 2017. Results prompted one key stakeholder to convey the "need to become a better destination for more consumers in higher income demographics." Such sentiment equally applies to the local market.

Macro factors played a role, but growth compares unfavourably to other channels

- Contracting industry sales occurred against a broader backdrop of weak wage growth, record indebtedness, low savings and soft confidence across Australian households.
- These enduring headwinds also inhibited overall national retail turnover growth, which dipped from a high of 3.3% in May to a low of 1.9% in October.
- P&C performance nevertheless compared unfavourably to overall national retail growth, and across IRI's four measured FMCG channels.
- The rate of growth was also lower than the store count increase (+2.1%); in other words, dollars per store trended downwards.

DOLLAR GROWTH BY FMCG CHANNEL, MAT TO 31/12/17

+1.0%
P&C

+2.7%
Total Retail*

+2.6%
Packaged Grocery

+3.4%
Liquor

+1.5%
OTC Pharmacy

Source: IRI MarketEdge; AACS Member Submissions; *Australian Bureau of Statistics

SITE STATISTICS OF RETAILERS USED IN CHANNEL MEASUREMENT

Retailer	2017	2016	Difference	% Difference
7-Eleven	675	645	30	4.7%
AA Holdings	52	53	-1	-1.9%
APCO	25	24	1	4.2%
BP	302	308	-6	-1.9%
Caltex All Star	656	654	2	0.3%
Coles Express	711	695	16	2.3%
Freedom Fuels	42	43	-1	-2.3%
Independents	750	743	7	0.9%
New Sunrise	687	646	41	6.3%
Night Owl	74	70	4	5.7%
On The Run (Peregrine)	140	137	3	2.2%
Puma Energy	213	221	-8	-3.6%
UCB	1,103	1,077	26	2.4%
United (including Distributors)	380	370	10	2.7%
Woolworths Petrol	533	527	6	1.1%
TOTAL	6,343	6,213	130	2.1%

Source: IRI MarketEdge; AACS Member Submissions; Company Websites

Food/Beverage

Dollar sales **$3.8 billion**

DOLLAR GROWTH YA %	ACTUAL GROWTH ($ MILLIONS)
+6.1% 2016	+$209m 2016
+2.5% 2017	+$91m 2017

Non-Food

Dollar sales **$4.6 billion**

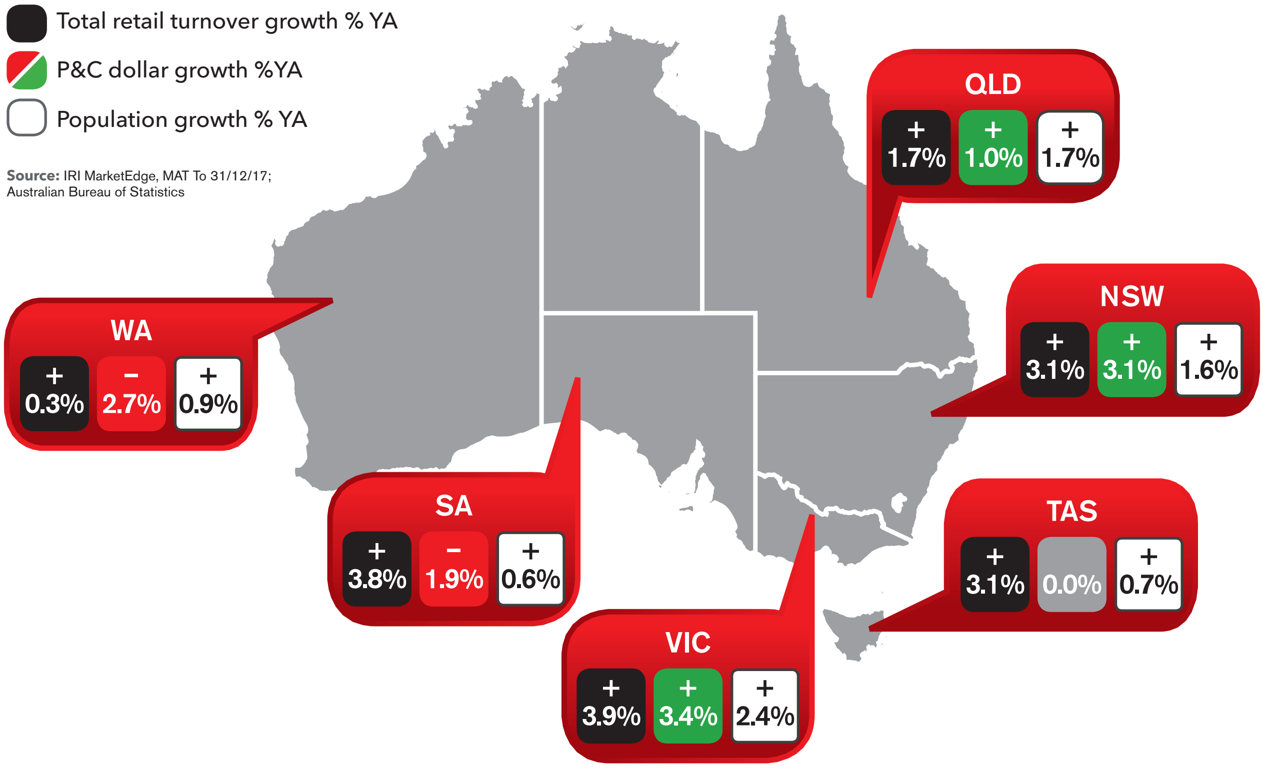
DOLLAR GROWTH YA %	ACTUAL GROWTH ($ MILLIONS)
+3.2% 2016	+$144m 2016
-0.1% 2017	-$6m 2017

SLOW

A pronounced slowdown in food, and negative non-food growth, inhibited industry revenues

- Food and beverage merchandise (+2.5%) outperformed non-food merchandise (-0.1%) for the third successive year.
- Non-food – having seen revenue growth plummet from 3.5% and 3.2% in 2015 and 2016 respectively – is an ongoing area of concern.
- Non-food added $144 million in 2016, but leaked -$6 million in 2017.
- The industry lost -$88 million in value from 3 non-food categories (communications, printed materials and travel tickets) – each having lost further relevance in physical retail.
- Food and beverages outperforming non-food items reflects a long-running position of AACS that a more progressive food offering underpins future industry success.
- Nevertheless, overall food and beverage product growth also contracted from 6.1% in 2016 to 2.5% in 2017 – a 59% drop in the annual growth rate.
- Established top-up/impulse fixtures like confectionery, ice cream, milk, and bread all declined – losing in excess of -$29 million in collective revenue.
- RTD beverage growth is showing challenging signs of price deflation, and an over-reliance on low price coffee to generate sales momentum.

TOTAL RETAIL REVENUE GROWTH, P&C DOLLAR GROWTH, AND POPULATION GROWTH, BY STATE, 2017



Source: IRI MarketEdge, MAT To 31/12/17; Australian Bureau of Statistics

The highest levels of dollar growth were observed in New South Wales and Victoria

- IRI's MarketEdge recorded dollar growth of 3.7% in NSW, following a 5.4% uplift in 2016.
- Declining growth in both South Australia (the fastest growing state in 2016), and Western Australia, inhibited national market performance in 2017.
- A contraction of -2.7% in Western Australia occurred despite recording the largest percentage increase in store account (+5.9%). Dollars per store per week declined -8.2%.
- The decline in South Australia (-1.9%) occurred in spite of a 1.1% increase in store count.
- Macro-economic and socio-demographic trends were influential; the 3 states where P&C sales grew also recorded the strongest YOY population growth.

VIC

The fastest growth was observed in Victoria, where IRI's scan banners increased sales by 3.4% (albeit down from 3.7% in 2016).

- Likewise, NSW and Victoria led Comsec's 'State of the States' report rankings due to the strength of each state's economic performance.
- Annual retail turnover growth was the strongest in Victoria, and above average in NSW, according to ABS data.

Concentrated growth among certain retailers and categories was again evident in 2017

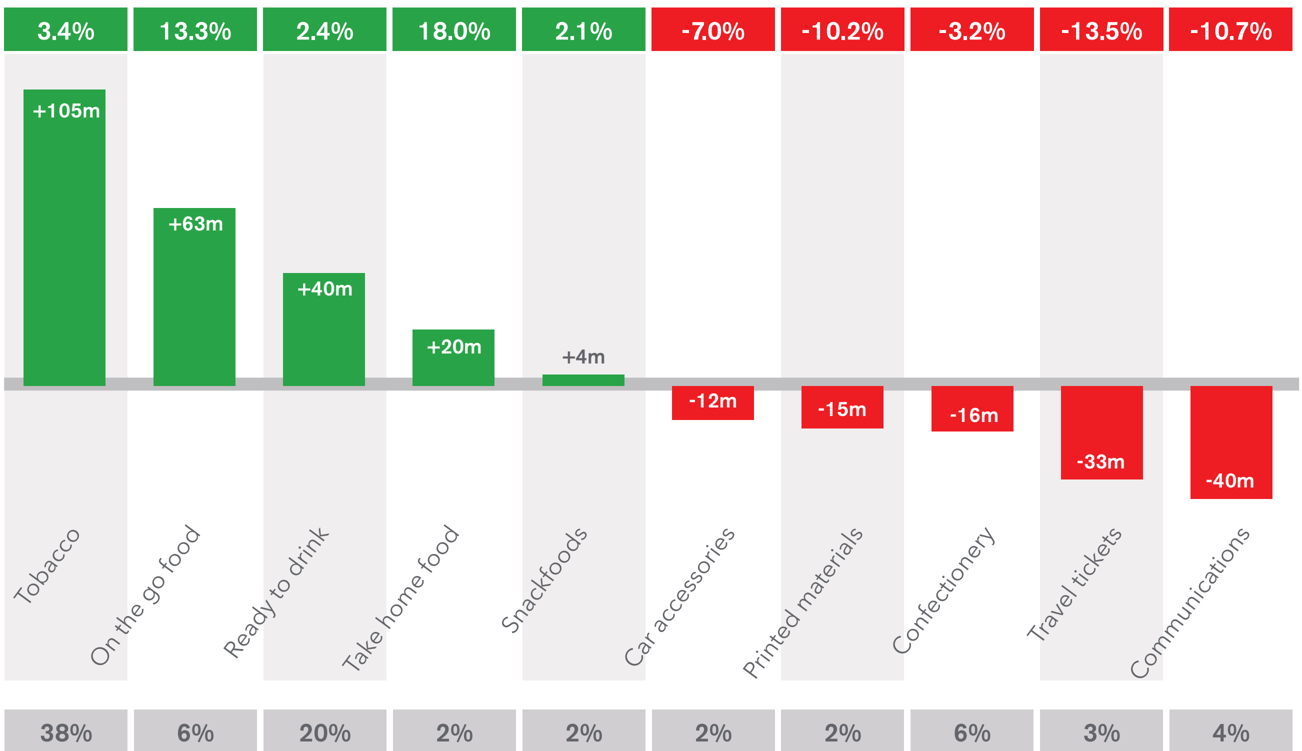
- Only 3 of the retail banners in IRI's MarketEdge grew sales revenues in 2017 – one of which overwhelmingly won share.
- And with 13 of the 20 categories declining, the industry was even more reliant on select high performing categories for growth.
- 2017 once again showed that the provision of (light) meals/anytime snacks via the surging on the go food category is propelling the industry forward.
- The same driving forces exist for the nascent take home food fixture, which accounted for a 24% share of all P&C dollar growth in 2017.
- RTD beverages accounted for 47% share of total industry dollar growth (versus 20% share) despite the category's annual rate of growth contracting.

Most significantly, the $105 million in additional growth derived from tobacco sales represented a 123% dollar share of total industry growth.

- Put another way, if tobacco was removed from the mix overall non-food items would have lost revenues amounting to -$111 million.

Top 5 dollar growth generating and declining categories in Australian P&C in 2017

Actual Dollar Growth (millions) and YOY growth (%), by category



Dollar share of P&C

Source: IRI MarketEdge; AACS Member Submissions

Convenience Channel Performance

Category	Value ($000,000s)	Share	2017 Growth	2016 Growth
Total Convenience	**8,396**	**100.0%**	**1.0%**	**4.5%**
Total Non Food	4,605	54.8%	-0.1%	3.2%
Total Food	3,791	45.2%	2.5%	6.1%
1				
Lotteries	16	0.2%	**33.3%**	231.8%
Take Home Food	131	1.6%	**18.0%**	8.9%
On The Go Food	538	6.4%	**13.3%**	18.3%
Tobacco	3,185	37.9%	**3.4%**	4.5%
Ready To Drink	1,695	20.2%	**2.4%**	5.2%
Snackfoods	194	2.3%	**2.1%**	6.9%
Medicinal	44	0.5%	**0.0%**	18.9%
2				
Take Home Beverage	310	3.7%	**-1.0%**	3.0%
General Merchandise	448	5.3%	**-2.4%**	19.6%
Ice Cream	162	1.9%	**-2.4%**	-3.0%
Confectionery	483	5.8%	**-3.2%**	3.6%
Grocery	92	1.1%	**-4.2%**	5.0%
Milk	146	1.7%	**-4.6%**	7.2%
3				
Bread	40	0.5%	**-4.8%**	4.3%
Personal Care	39	0.5%	**-4.9%**	2.6%
Household	35	0.4%	**-5.4%**	11.3%
Car Accessories	159	1.9%	**-7.0%**	-2.0%
Printed Materials	132	1.6%	**-10.2%**	-8.2%
Communications	335	4.0%	**-10.7%**	-11.7%
Travel Tickets	212	2.5%	**-13.5%**	-5.0%

Source: IRI MarketEdge; AACS Member Submissions

TOBACCO

Dollar sales
$3.2 billion

DOLLAR GROWTH YA %
+4.5% 2016
+3.4% 2017

ACTUAL GROWTH
+$105 million 2017

Dollar share
37.9%

Margin
25.6%

Tobacco's dollar growth slowed as volume sales (units and sticks) decelerated further

- Just under 38 cents of every dollar spent in P&C stores in 2017 was tobacco related.
- IRI's MarketEdge shows that 3 of the industry's top 5 dollar growth generating segments herald from tobacco; nearly 29% of all industry sales derive from tobacco's 2 largest segments.
- Tobacco dollar growth of 3.4% was down from the 4.5% uplift recorded in 2016.

Tobacco was a $3.2 billion category generating $105 million in additional value

- Despite slowing, tobacco's contribution to overall industry growth was even more significant in 2017 (due to challenges facing other non-food categories).
- IRI's MarketEdge recorded tobacco unit sales were again down (-2.9%) at a rate comparable to 2016, but a more pronounced decline in stick volumes (-3.9% versus -1.2% in 2016) occurred. This is indicative of the accelerated shift to smaller pack size format in P&C as a means to manage dollar outlay.
- Excise driven price per unit increases of 7.2% propelled value growth.
- Tobacco users have absorbed a near 16% unit price increase from 2015-17 in products purchased in P&C stores.
- Average dollars per stick grew from 0.70 cents in 2015 to 0.80 cents in 2017 – a 15% uplift.

TOBACCO'S TOP 3 AND BOTTOM 2 GROWTH PRODUCT SEGMENTS, 2016 & 2017

	Dollar share	Dollar growth YA %		Unit growth YA %	
		2016	2017	2016	2017
Sub value cigarettes	43%	+29.2%	+16.5%	+14.4%	+6.8%
Roll your own	9%	+15.3%	+10.4%	+9.6%	+3.7%
Value cigarettes	4%	-30.7%	+19.1%	-35.1%	+30.5%
Premium cigarettes	11%	-14.2%	-9.5%	-21.6%	-17.1%
Mainstream cigarettes	33%	-3.4%	-6.7%	-12.3%	-17.0%

Source: IRI MarketEdge, MAT To 31/12/17

Sub value cigarettes and roll your own (RYO) again led tobacco growth

- Sub value cigarettes generated 43% of all tobacco dollars – up 12 percentage points in just 2 years; the segment also accounted for 4 of the top 5 growth driving tobacco brands.
- Only one retailer in IRI's MarketEdge scan read failed to record double-digit gains in sub value cigarettes.
- The top 2 growth driving tobacco brands in IRI's market measurement were both sub-value offerings, which collectively contributed over $100 million in added value in 2017.
- The surge in sub-value cigarettes reflects tobacco consumers continuing to trade down against a backdrop of excise increases.
- The same underlying motivation underpins the double-digit dollar increase in RYO tobacco – a format that resonates with price driven buyers.

Following years of double-digit increases, sub value cigarettes was again the largest dollar generating product segment across the P&C industry following a 17% increase.

- Both sub value and RYO segments recorded slower growth than in prior years, which was indicative of tobacco's slower annual growth.
- The established slowdown in mainstream cigarettes intensified, whereas the deceleration in premium cigarettes (-10%) was less pronounced due to sub-category price rationalisation and product developments.

Illicit trade continues to have a detrimental impact on the community and industry operators

For too long, illegal tobacco products with no quality control standards have been sold with impunity in the community.

> "Convenience store owners and staff know first-hand the impact that excise increases and regulations like plain packaging have had on the market for illegal cigarettes. The regulatory environment for legal tobacco in Australia has made us one of the world's most lucrative markets for organised criminals involved in the illicit tobacco trade"
>
> Jeff Rogut, AACS CEO

- KPMG's Illicit tobacco report published in March 2017 estimated that 13.9% of total Australian tobacco consumption was illicit (versus 11.5% in 2012).
- The ongoing significance of illicit trade is in spite of the Australian Border Force's tobacco strike team seizing 104 tonne of smuggled tobacco and 233 million smuggled cigarettes since being established in October 2015.
- AACS considers KPMG's estimate to be conservative based on direct and ongoing engagement with Border Control personnel who are closer positioned to the issue.
- But if the 2.3 million kg of illicit tobacco estimated by KPMG had been consumed legally, it would have represented an estimated excise value of $1.61 billion.
- Some P&C stores are losing up to $1,000 a week on a product that is typically the most profitable thing being sold by law-abiding and responsible operators.
- Adding to the burdens experienced by retailers are the higher insurance costs and additional security requirements they must have in place.
- Meanwhile, products such as eCigarettes, which are viewed internationally as vastly safer than tobacco smoking, and have the capacity to help people quit, remain unable to be legally sold.

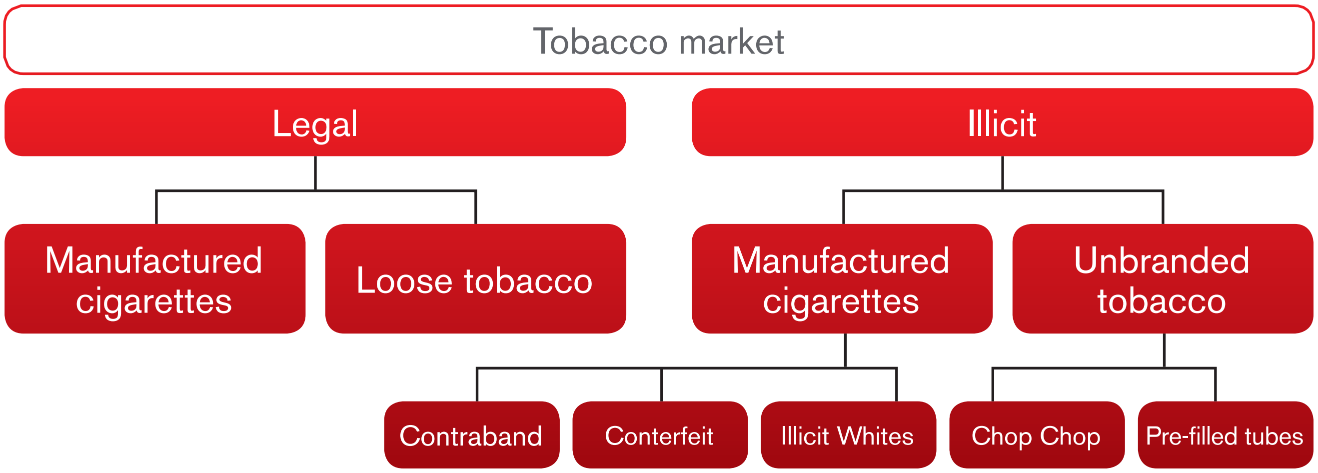
Excise policy has been an inadvertent boon to illicit trade for much of the last decade

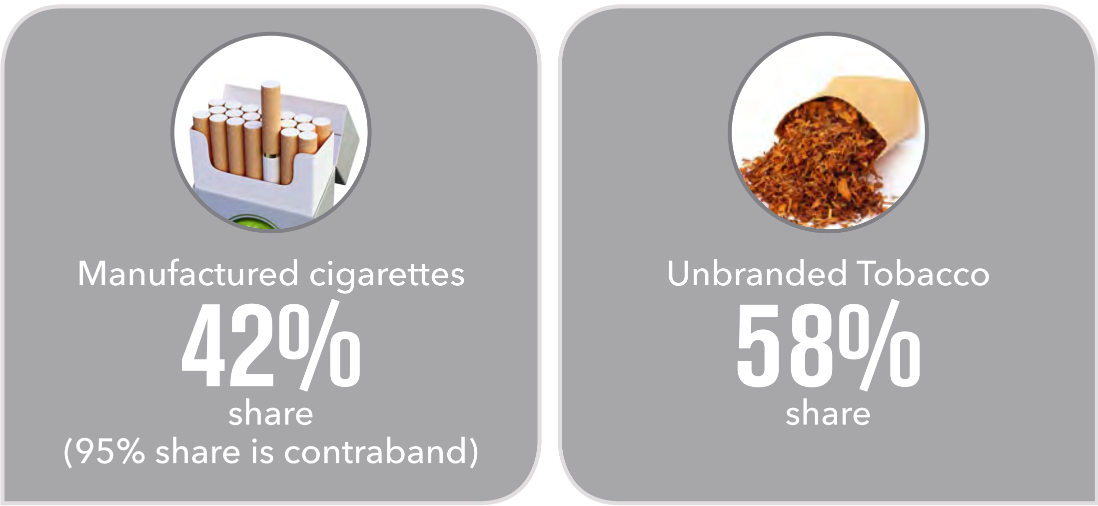
- As well as pinpointing the worryingly high proportion of illicit trade, KPMG's report noted how excise increases have resulted in a decline in relative affordability.
- Normally law-abiding smokers, who are/were already trading down to the sub value category, are being enticed into buying cheaper illicit products.

With no genuine country of origin, no quality control standards – and no idea what these products contain – consumers may be putting themselves at more risk than they realise.

- A large price differential between Australia and other nearby markets created an economic incentive individuals already undeterred by the sub-optimal penalties of being caught.
- The price differential between illicit and legitimate tobacco products has not varied much YOY from 2013-16; in other words, illicit operators are being financially incentivised.
- Stopping the importation, possession, purchase, sale and production of illicit tobacco through comprehensive legal measures is required.
- An encouraging development in early 2018 was the Government proposing to introduce penalties of up to 10 years in prison for manufacturing illicit tobacco.

> "We know that the illegal activities are going to ramp up every time we ratchet the duties and excises up. Every time that lawful cigarettes become more expensive there'll be greater and greater black market activity. AACS does nonetheless commend Liberal MP Craig Kelly for formally recognising the huge impact the illicit trade of tobacco is having on the community and on small businesses"
>
> Jeff Rogut, AACS CEO





Source: Adapted from KPMG

FOOD

On the go food

Dollar sales
$538 million

Dollar share
6.4%

DOLLAR GROWTH YA %
+18.3% 2016
+13.3% 2017

ACTUAL GROWTH
+$63 million 2017

Margin
38.7%

Continued double-digit growth in on the go food reflects retailer investment

- On the go food sales surpassed $0.5 billion in 2017 following annual dollar growth of 13.3%.
- The additional $63 million in growth was 69% of all additional food and beverage dollar growth.
- The category leapfrogged confectionery as the industry's largest food specific revenue generator following annual dollar gains between 13-18% in each of the past 3 years.
- Dollar growth has exceeded 12% for the past 8 quarters; the 15.9% uplift in Q4 2017 was the highest quarterly increase of the year.
- Robust growth is occurring despite intensifying competition from QSRs and online food delivery platforms (e.g. UberEats).
- Continued growth momentum is a story of retailer investment as supply chains bring "new news" to the category, making it a key destination mission outside of fuel.
- 5 of the top 10 growth contributing category SKUs were newly introduced products in 2017; more broadly, 20 of the top 50 SKUs were NPDs.
- Retailer investment to create a unique destination driving food offer has underpinned the significant role of private label in the category.
- Private label accounted for over half of category sales in IRI's MarketEdge measurement, and grew 20% (albeit down from the 34% increase in 2016).

The category accounted for 6.4% of total industry sales – up 1 percentage point in just 2 years.

The three key areas of on the go food merchandise recorded largely consistent growth

- IRI's MarketEdge showed the 3 key product segments, which collectively accounted for over 85% of on the go food dollar sales, sustained an upward growth trajectory.
- Sandwiches (+18.8%), fresh cakes (+16.9%), and hot pastries (+8.1%) performed well again, albeit with slightly reduced rates versus 2016.
- Sandwiches growth continued to over-index; share of dollar growth was 8 percentage points higher than dollar share (after being 14.5 percentage points higher in 2016).
- Sandwiches comprised the 12th largest revenue generating segment across the entire in-store mix, but was the 4th largest growth segment.
- Improved affordability/price perception has been important. IRI's MarketEdge shows that packaged sandwich prices have fallen by 10% over the last 2 years (-8% in 2017 alone).
- Meanwhile, fresh cakes and hot pastries were the channel's 6th and 7th largest growth generating segments respectively in 2017.
- Unit sales growth of fresh cakes slowed in 2017, but the impact was largely offset by a price per unit increase above 4%.

"The category's performance is ongoing evidence that the P&C industry has successfully adapted and focused on providing a stronger on-the-go food offer and food services. To have continued credibility as a sought after food 'destination,' P&C operators must invest in the quality, variety, health and freshness of the offer. Competition for breakfast, lunch and dinner spend across channels has never been fiercer as supermarkets, QSRs, cafés, bakeries, restaurants and delis evolve their 'on-demand' food offers. But our industry can lead the way"

Jeff Rogut, AACS CEO

- Hot pastry prices dipped -2.4% as the segment's unit growth (+10.3%) exceeded dollar growth (+8.1%).
- Foodservice products also performed well (+24%) due to new sushi and burrito items.
- The rise of ethnic, street food themed formats is likely to be a key category growth theme moving forward as innovation helps the retail experience feel less of a sterile environment.
- There is still work to be done; Convenience Measures Australia shopper research shows that on the go food has the lowest Net Promoter Score (NPS) of all measured categories. And the category is still only represented in one-in-five baskets.

PERFORMANCE OF THE CATEGORY'S TOP GROWTH DRIVING PRODUCT SEGMENTS, 2016 & 2017

	Dollar share	Dollar growth YA %		Unit growth YA %	
		2016	2017	2016	2017
Hot Pastry	41%	+11.2%	+8.1%	+9.4%	+10.7%
Sandwiches	29%	+26.0%	+18.8%	+28.0%	+28.6%
Fresh Cakes	21%	+22.0%	+16.9%	+22.0%	+12.1%
Foodservice	9%	-2.5%	+23.8%	-1.9%	+30.4%

Source: IRI MarketEdge, MAT To 31/12/17

On the go food gains were not realised equally across all retailers

- IRI's MarketEdge shows that three retailers recorded dollar growth above 20%; others recorded single-digit gains, and a few saw marginal declines.
- In May 2017, 7-Eleven Australia – which generates 190 million transactions per year – emphasised it was "experiencing strong growth and "wants to be known for new and exclusive products, and famous for food on the go."
- More recently in January 2018 the retailer said that "more and more customers trying and enjoying our 7-Eleven brand food on the go which has led to strong sales growth."
- Performance has arguably been propelled by building a business model around convenience first and foremost, and petrol second.
- For Coles Express, "strong growth in food-to-go offering" was a headline message for its convenience business in the 2018 half-yearly results.
- It is perhaps telling that Coles Express and 7-Eleven led consumer perception in Canstar's Petrol & Service Stations satisfaction research.
- Being the only operators to receive a 5-star rating for 'range of items on sale' indicates how effective food to go ranging can impart a broader halo on store brand perception.
- Recognising this, Caltex's long-term 'Freedom of Convenience' project has resulted in 23 pilot Foodary stores opening (by 31 December 2017), and another 50-60 expected in 2018.
- Caltex saw "strong customer acceptance of fresh food, barista coffee offer; QSR partnerships established" according to its annual trading statement.

7-Eleven's "strong sales growth" has been supported by rotating food product promotional activity that drives footfall day-to-day, and by daypart . It is also among leading retailers using engaging and dynamic LED screens to optimally showcase occasion-based food offers.

rotating promotions

Adaptation of QSR models in the convenience space: 7-Eleven's approach is not dissimilar to the approach taken by QSR's like Subway, but instead has more varied merchandising mix to draw upon (which could even lead to party platters in future).

Take home food

Dollar sales
$131 million

Dollar share
1.6%

DOLLAR GROWTH YA %
+8.9% 2016
+18.0% 2017

ACTUAL GROWTH
+$20 million 2017

Margin
32.0%

Take home food (THF) sales accelerated again in 2017

- THF accounted for 1.6% of total industry sales in 2017 following YOY dollar growth of 18.0%.
- One brand gaining prominence is YouFoodz, a ready-to-eat meal service that is seeing improved distribution of its ready meals in retail outlets across channels.
- YouFoodz added nearly $2 million in added value in 2017 according to IRI's MarketEdge measurement – second only to the Krispy Kreme brand in THF growth contribution.
- Over 16,000 online YouFoodz reviews generated an average user rating of 4.4 (out of 5), which shows how modern and quality focused prepared meals can entice time-poor Australians.
- Just over a fifth (21%) of THF sales in 2017 (per IRI's scan measurement) were private labels, with dollar growth up 30% (versus a near –7% decline in 2016).

The $131 million category added $20 million in actual dollar growth, driven by a wide assortment of products ranging from larger Krispy Kreme donut packs to ready meals.

youfoodz

Youfoodz sales in P&C stores measured by IRI grew above 800% in 2017. Ranging such brands that are premium, convenient and healthy supports the gradual repositioning of convenience stores. It also supports the industry's transition beyond typical demographics (young, male, tradesmen) towards enticing more females, professionals, and older customers.

Youfoodz Dollar Growth

>800%

7-Eleven's foray into ready meals propelled 20% plus growth in private label take home items . It could prove to be a catalyst for heat-and-eat meals to secure an elevated role in the channel, private label or not.

Private label

>20%

Caltex empowers customers to determine value on their own terms with multi-item meal deals.

Customers determine

value

Source: IRI MarketEdge; 7-Eleven; Caltex

Bread

Dollar sales
$40 million

Dollar share
5.8%

DOLLAR GROWTH YA %

+4.3% 2016

-4.8% 2017

ACTUAL GROWTH

-$2 million 2017

Margin
32.4%

Bread sales declined for the first time in a number of years

- The $40 million bread category recorded mid single digit declines in 2017, puncturing at least 3 successive years of growth.
- Lower private label sales (down -4.4%) set the tone for the category's diminishing sales.
- With Australians doing more top-up shops (as evidenced by strong supermarket transaction growth), centre-store P&C sales may suffer further.
- Meanwhile, high single-digit growth in the supermarket's in-store bakery products coexists with retailers aspiring for a 'destination driving' perimeter store space.
- Even Aldi is now beginning to prioritise fresh produce and bakery items in store renewals, and newly opened stores throughout Australia and internationally.
- And then there is the broader competitive environment of a thriving foodservice scene where higher income consumers embrace specialty bakery items for at-home use.

Coles announced in mid-2017 that it wanted to be famous for its fresh bread, and intends to aggressively roll out more in-house bakeries accordingly

Confectionery

Dollar sales
$483 million

Dollar share
5.8%

DOLLAR GROWTH YA %

+3.6% 2016

-3.2% 2017

ACTUAL GROWTH

-$16 million 2017

Margin
49.1%

Confectionery lost ground due to declines in the category's three key product formats

- Confectionery sales fell well below $0.5 billion following a reversal in fortunes in 2017.
- Dollar growth of 3.6% in 2016 was followed by a -3.2% decline in 2017 (-$16 million).
- Contracting sales was widespread across a majority of retailers; only 2 IRI scan banners recorded YOY dollar growth and only 1 banner sold more units.
- Sugar confectionery and chocolate confectionery both recorded declines exceeding -3%.
- Hang-sell sugar confectionery items were down -5.5% in IRI's MarketEdge measurement where accelerated dollar declines (-5.7%) in mints was also observed.
- Medium-sized chocolate bars continued to lose sales at a double-digit rate (-14.7%), while king-size bars fell into decline too (-2.1%).

In chocolate, block formats emerged as the most significant bright spot owing predominately to the format extension of M&Ms.

- Gum sales also reversed; 4.4% growth in 2016 was followed by a marginal decline of -0.7% in 2017 in a segment that has relied heavily on Wrigley to generate gains in recent times.
- Unit growth performance in gum continues to be inferior to dollar growth because of larger 46 pellet packs again having a larger influence in the segment's sales mix.

Category management is a challenging and important process

- Confectionery is generally responsive to, and reliant on, innovation; two of the top 3 value adding brands were NPD's (or brand extensions) from Cadbury and Mars.
- All of the top 8 value adding items in the category in 2017 were new products.
- However, much of the innovation has not been incremental – at least in the P&C channel.
- Many high performers have been offset by declines in an adjacent product offering under the same masterbrand. Or high performers of 2016 didn't lap performance in 2017.
- Indeed, the top 3 value adding brands of 2016 all fell into decline in 2017, with many of the top selling brands (including private label) posting declines.

Some consistent growth drivers have emerged in the last 2 years: Kinder Bueno has recorded dollar growth upwards of 30% for successive years; Mars Pods and Extra Fruit Pellet have also recorded successive years of double-digit dollar growth.

PERFORMANCE OF THE CATEGORY'S 3 KEY PRODUCT SEGMENTS, 2016 & 2017

	Dollar share	Dollar growth YA %		Unit growth YA %	
		2016	2017	2016	2017
Chocolate Confectionery	57%	+5.0%	-3.2%	+0.8%	-1.8%
Sugar Confectionery	28%	+0.3%	-3.3%	-1.4%	-2.2%
Gum	14%	+4.4%	-0.7%	-1.3%	-5.9%

Source: IRI MarketEdge, MAT To 31/12/17

Snackfoods

Dollar sales
$194 million

Dollar share
2.1%

DOLLAR GROWTH YA %

+6.9%
2016

+2.1%
2017

ACTUAL GROWTH

+$4 million
2017

Margin
48.2%

Snackfoods growth softened in 2017 but continues to outperform the industry average

- The traditional three meal routine per day is being reduced and going towards frequent grazing/snacking. Highlighting this, just 21% of IRI's Shopper Panel subscribe to the notion that they "eat three square meals and no snacks."
- Nevertheless, snackfoods dollar growth of 2.1% in 2017 was down from 5.7% and 6.9% in 2015 and 2016 respectively. This amounted to $4 million in additional sales revenue.
- Retailers experienced varying fortunes with two banners recording mid single-digit declines, and one retailer generated growth just under 14%.
- IRI's MarketEdge captured a pronounced slowdown at the year-end; double-digit growth in Q4 2016 could not be lapped in the equivalent quarter of 2017 when revenues dipped -1.4%.
- Product counts across each of the key category segments either declined or slowed versus 2016 in IRI's scan measurement.

The snackfoods category has become a symbol of how the channel is providing a more balanced product mix to satisfy both customer needs of health and indulgence.

Nevertheless, the $194 million category – consisting of chips, nuts, popcorn, nutritional bars, dried fruit, and pretzels – slowed in 2017.

SLOW

Worsening performance in chips and popcorn led to slowing category growth

- Chip revenues fell into marginal dollar decline and accounted for 4 of the bottom 5 brands posting the most significant declines.
- Sales have likely been cannibalised by the grocery channel where the chips category has been outperforming the packaged grocery average.
- In P&C there has arguably been too much reliance on price-pack-size adjustments and not enough truly disruptive innovation to capture the hearts and wallets of shoppers.
- Following 2 consecutive years of triple-digit growth, popcorn dollar growth slowed to 5.5% and units sold declined amid a segment price increase of 7.1%.
- Nutritional bars (+13.8%) and nuts (+7.5%) recorded robust growth, albeit a deceleration versus 2016 levels.
- Good/better-for-you snacking options recording such robust growth is evidence of consumers utilising snacks to get the nutritional boosts they need throughout the day.

Popcorn's slowdown was influenced by another year of sales declines for the segment's leading brand (Cobs), and a notably less pronounced private label influence.

PERFORMANCE OF THE CATEGORY'S 4 KEY PRODUCT SEGMENTS, 2016 & 2017

	Dollar share	Dollar growth YA %		Unit growth YA %	
		2016	2017	2016	2017
Chips	**65%**	**+2.9%**	**-0.7%**	**+2.3%**	**+0.6%**
Nutritional bars	**18%**	**+20.9%**	**+13.8%**	**+13.9%**	**+12.0%**
Nuts	**12%**	**+10.6%**	**+7.5%**	**+3.3%**	**+7.9%**
Popcorn	**5%**	**+131.3%**	**+5.5%**	**+155.7%**	**-1.5%**

Source: IRI MarketEdge, MAT To 31/12/17